Internal Revenue Service

memorandum

CC:INTL-0390-89
Br1:RJMisey

date: JUN 25 1990

to: Paul G. Topolka, Special Litigation Assistant
District Counsel - Greensboro

from: Chief, Branch 1
Associate Chief Counsel (International) CC:INTL:1

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subject: [redacted]

Facts:

From [redacted] to [redacted], [redacted] entered an agreement allowing [redacted] (hereinafter "[redacted]") to drill for oil. From [redacted] to [redacted], [redacted] broke the agreement, raising the posted price of oil before finally nationalizing the assets of [redacted] in [redacted].

Claiming it was damaged, [redacted] submitted its dispute with [redacted] to an arbitration board on [redacted]. Pursuant to the arbitration agreement, each party selected a member of this three person board and the International Court of Justice appointed the final member. On [redacted] the board awarded [redacted] dollars, vaguely classifying [redacted] dollars of the award as the "inflation factor." While the Service believes that the inflation factor constitutes interest which is ordinary income, [redacted] claims that the inflation factor constitutes part of the amount realized on the nationalization, against which it may take a capital gains deduction.

Trying to clarify the matter, [redacted] wrote the President of the arbitration board, [redacted]. [redacted] responded with a letter supporting [redacted] by stating that the board intended the inflation factor to be compensation for the taking.

Issue:

Do the Federal Rules of Evidence allow [redacted] to introduce either the [redacted] letter or the testimony of [redacted] as evidence in support of its claim?

Conclusion:

The Federal Rules of Evidence do not allow [redacted] to introduce the [redacted] letter, which is heresay. Substantial case

law indicates that [redacted] can introduce the testimony of [redacted].

Analysis:

The [redacted] letter is not admissible because it is heresay. Heresay is a statement made by the person who is not testifying that is offered to prove the truth of the matter asserted. Because the letter is a statement about the issue by an individual who is not testifying, it is heresay.

As heresay, the letter is inadmissible unless it falls within an exception. In this matter, the closest exception is Rule 803(8).

Rule 803(8) admits heresay statements of public agencies regarding the activities of the office or agency. The rationale behind the public office or agency requirement is that if the statement was made pursuant to a duty imposed by law, it has the reliability inherent in official records and avoids the necessity of bringing public officials into court.

The Rule 803(8) exception does not save the letter because the arbitration board is not a public office or agency. The case law involving Rule 803(8) has not dealt with whether the exception applies to so-called "ad hoc" officials. Here, the [redacted] letter regards the activities of the arbitration board. If the arbitration board is a public office or agency, the heresay exception applies and [redacted] may introduce the [redacted] letter. If the arbitration board is not a public office or agency, the heresay exception does not apply and [redacted] my introduce the [redacted] letter. The arbitration board existed due to an agreement between [redacted] and [redacted]. Although the International Court of Justice appointed the final member, the arbitration board did not report to it or to any other governmental instrumentality. Therefore, we conclude that the arbitration board was not a public office or agency.

However, [redacted] may introduce the testimony of [redacted].

[redacted]'s testimony is relevant because it is probative of the interpretation of the arbitration award. Rule 401. Furthermore, his testimony is not heresay because he will actually be in court.

Your memorandum raises the possibility of excluding his testimony pursuant to Rules 605 and 606. Both of these rules are inapplicable.

Rule 605 states that "[t]he judge presiding at the trial may not testify in that trial (emphasis added) as a witness."

Although [redacted] was the President of the Arbitration board, he was not a judge. In addition, the Rule specifically refers to the trial at which the judge is presiding - not a later trial.

Because [redacted] clearly was not a juror, Rule 606 is irrelevant.

An analysis of the case law provides authority that judges may testify in later trials.

The Tax Court has allowed judges from former trials to testify in an attempt to clarify the issues raised and decided when the record of the former trial is ambiguous. Cook v. Commissioner, 80 T.C. 512 (1983). Although the typical case where this occurs involves a divorce court judge explaining his divorce decree, we think the Tax Court will similarly allow an arbitrator to testify. See also Schumert & Warfield v. Security Brewering Co. (La. 1912).

We recommend that you try to reach the other two members of the Arbitration board to support your position that the inflation factor constitutes interest.

Although you did not request our advice on the substantive legal issue, we reviewed the report of the International Examiner, Paul Tew, and concur in his opinion that the inflation factor is interest.

If you have further questions, please contact Rob Misey at (FTS) 287-4851.

George M. Sellinger
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